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MAY 15 1998

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket Nos. 96-45/97-160
Federal State Board on	)	DA 98-715
Universal Service	)	

COMMENTS OF GTE

Dated: May 15, 1998

GTE Service Corporation and its affiliated domestic telephone operating, wireless, and long distance companies

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EXECUTIVE SUMMARY

GTE sets forth three necessary requirements against which any proposal for a Federal universal service support mechanism must be tested. *First*, the Federal plan must provide new, explicit support that is sufficient to replace the implicit support generated by current interstate access charges. *Second*, the Federal plan must provide a reasonable amount of new support to states to replace the implicit support provided by intrastate access, toll and vertical services. *Third*, the Federal plan must maintain the explicit support that is provided by the existing Federal high cost fund.

GTE urges the Commission to adopt a cost model and the inputs to be used prior to selecting the benchmarks and percentages that will distribute responsibility for universal service support among the Federal and states' plans. GTE also recommends that the Commission adopt a surcharge based on total (interstate, intrastate and international) retail revenues as the appropriate basis for both the contribution method and recovery mechanism. GTE stresses that the benchmark should be characterized as a "cost" benchmark designed to satisfy the three requirements. The benchmark should not be selected or calculated based upon either an average cost or revenue because, among other reasons, there is no assurance that such a benchmark will produce and target sufficient support.

GTE's proposal is the only plan before the Commission that provides the flexibility the Commission will require to assure that the calculated support will be reasonable and sufficient to achieve the three objectives once the cost model and inputs are selected. Parties presenting other proposals have either failed to evaluate their proposals against any measurable criteria, or have selectively emphasized one requirement while ignoring others.

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COMMENTS OF GTE

GTE Service Corporation and its affiliated domestic telephone operating, wireless and long distance companies[1] (collectively, "GTE") respectfully respond to the Common Carrier Bureau's Public Notice DA 98-715 ("Notice") seeking comments on proposals to revise the Commission's methodology for determining universal service support.

I. TO SATISFY THE REQUIREMENTS OF THE TELECOMMUNICATIONS ACT OF 1996 ("ACT"), THE FEDERAL PLAN MUST MEET SPECIFIC REQUIREMENTS.

In its Proposal, GTE set forth three necessary requirements that the Federal universal service mechanism must achieve regardless of the specific cost model or

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1 These comments are filed on behalf of GTE's affiliated domestic telephone operating companies, GTE Wireless Incorporated, and GTE Communications Corporation, Long Distance Division. GTE's domestic telephone operating companies are: GTE Alaska Incorporated, GTE Arkansas Incorporated, GTE California Incorporated, GTE Florida Incorporated, GTE Hawaiian Telephone Company Incorporated, The Micronesian Telecommunications Corporation, GTE Midwest Incorporated, GTE North Incorporated, GTE Northwest Incorporated, GTE South Incorporated, GTE Southwest Incorporated, Contel of Minnesota, Inc., and Contel of the South, Inc.

The submission of these Comments in no manner prejudices GTE's positions set forth in its appeals of the Commission's universal service and access charge reform orders. *See* GTE's Proposal, filed April 27, 1998, at 1 n.1.

benchmarks used in the Federal high-cost support calculation.[2] Several parties that have submitted proposals also recognize the necessity of these requirements, but some parties emphasize one of the requirements in preference to the others. The three requirements are:

First, the Federal plan must provide new, explicit support that is sufficient to replace the implicit support generated currently within interstate access charges.[3] BellSouth (at 2) correctly recognizes the need to maintain at least the current level of support, which is provided today through a combination of implicit and explicit means. BellSouth's proposal (at 3) would determine Federal support, in part, by calculating the amount of implicit support provided through interstate access. Sprint also proposes (at 5) that the new explicit funding must be sufficient to replace the current implicit support, so that implicit universal service support can be eliminated. In addition to providing sufficient explicit funding overall, the Federal plan also must target explicit support accurately to non-rural company areas in a pattern that approximates the current pattern of implicit support. Otherwise, it will not be possible for each company to effectuate appropriate offsetting reductions to its interstate access rates.

Second, the Federal plan must provide a reasonable amount of new support to the states to replace support that is provided implicitly today by intrastate rates for

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[2] As emphasized in GTE's Proposal, prior to selecting specific benchmarks and percentages that will determine Federal and state responsibilities for universal service support, the Commission should first adopt a cost model and inputs. This methodical approach will assure that, once calculated, the support amount will be reasonable and sufficient.

[3] GTE at 14.

services such as access, toll, and vertical services.[4] The need for Federal high-cost assistance is greatest in states that have relatively high costs and/or a relatively small base of revenues. Several parties, including South Dakota (at 2-4), US West (at Attachment 1), and the Ad Hoc Working Group (at 1) emphasize the necessity to provide Federal funding to address state needs. In designing the Federal plan to meet this requirement, the Commission must strike a reasonable balance between the interests of high and low cost states. As with the first requirement, the framework chosen for the Federal fund must allow the Commission to select the appropriate total amount of this support, and also to distribute that support among the states in the requisite pattern. South Dakota and Colorado both propose the addition of new parameters to the Federal calculation to allow support to be targeted to states which are most in need.[5]

Third, the Federal plan must maintain the explicit support that is provided today by the current high cost fund ("HCF").[6] The plan adopted by the Commission in May 1997 ("May 1997 plan") maintains this support for rural companies for three years, but eliminates support to the states under the current HCF in areas served by non-rural

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4 GTE at 15.

5 South Dakota (at 2-3) recommends state-specific benchmarks, and Colorado (at 2-3) propounds a variable percentage for funding by the Federal jurisdiction. Colorado effectively contemplates a variable state benchmark as well in its" dead band" approach (at 3).

6 GTE at 18.

companies. At a bare minimum, the new Federal plan must "do no harm" in the sense that no state should face a *greater* universal service burden than it does today.[7]

Meeting these three requirements is not optional, but rather necessary to target sufficient, explicit funding accurately to carriers that undertake universal service obligations.[8]

II. GTE'S PROPOSAL WOULD PRODUCE A FEDERAL PLAN THAT SATISFIES THE REQUIREMENTS NECESSARY TO MEET THE STATUTORY IMPERATIVES OF SECTION 254 OF THE ACT.

The framework proposed by GTE would allow the Commission to construct a Federal plan that meets the necessary requirements enumerated above. Since the Commission has yet to adopt a cost model and inputs to size the Federal universal service fund, GTE has proposed a broad framework for a sufficient Federal plan rather than specific benchmarks and percentages.[9] GTE strongly urges the Commission to adopt a cost model and inputs *before* attempting to finalize the parameters of the support calculation. Otherwise, the Commission cannot assure that the calculated support amount will be reasonable. The Commission would then choose a sliding scale

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7 *See, e.g.*, BellSouth (at 3), PRTC (at 2), and Ad Hoc (at 21).

8 There are several additional tasks that the Federal mechanisms must perform, but which are not discussed in detail in these comments. In particular, *first*, the current level of HCF and long term support ("LTS") must be maintained for rural companies over the next three years. *Second*, the Lifeline and Linkup programs must be funded. And, *third*, the Federal programs for schools, libraries, and health care providers must be paid for. These are not discussed here because the amounts needed for these purposes are not determined by the non-rural funding calculation which is the subject of the instant Notice.

9 GTE's Proposal provided illustrative examples to demonstrate how the fund parameters (benchmarks and percentages) could be adjusted to achieve the desired policy goals. See GTE's Proposal at 23-25 and Attachment A.

of benchmarks and percentages that produce funding amounts that satisfy the necessary requirements, both in total and by state.

Under GTE's Proposal, the amount of HCF currently provided in each non-rural study area would be passed through to the state through the Part 69 allocation process, as it is today. The plan would thus satisfy the third requirement, that the current flow of HCF funding should be maintained.

The amount of new Federal support provided to each study area, net of the existing HCF support amount, would then be applied toward reductions in the non-rural company's interstate access rates. These rates would be reduced until the funds were depleted, or until a reference level established by the Commission was achieved. The plan would thus satisfy the first requirement, that the implicit support provided by interstate switched access would be replaced by explicit support from the Federal universal service mechanism.

Finally, if, in a given study area, interstate access rates were reduced to the reference level established by the Commission, any remaining dollars of Federal support, not yet applied toward interstate access reductions, would be flowed to the state. This would be done using the same pass-through mechanism in Part 69 that is used for HCF support today. The Commission would require that the state use these funds to make offsetting reductions in the company's rates for intrastate services that provide implicit support today, but would leave the specific reductions to be determined by the state. The benchmarks and percentages would be chosen so that, given the cost model estimates, this procedure would send a reasonable amount of this new Federal support to those states where it is needed. The proposal would therefore meet the second requirement, that the Federal plan should provide an amount of new Federal support to the states that would represent a reasonable balance among the concerns of low and high cost states.

Under GTE's Proposal, the plan would apply Federal support dollars first to maintain the current HCF support, then to replace implicit support in interstate access, and finally to provide additional funding to states with high costs and/or low revenue bases. In this sense, the support would be applied in a "cascading" process analogous to the manner in which common line revenues today are recovered first from SLCs, then from PICCs, and finally from CCL charges.

III. THE PLANS PROPOSED BY VARIOUS PARTIES DO NOT MEET THE NECESSARY REQUIREMENTS.

Parties acknowledge that if the requirements enumerated above are not met, the imperatives of Section 254of the Act will not, and cannot, be satisfied. If some portion of universal service support remains implicit solely in the service rates of incumbent local exchange carriers (ILECs), clearly not all telecommunications providers will contribute towards universal service on an "equitable and nondiscriminatory" basis as mandated by Congress. As Sprint highlights (at 2), the development of local competition depends critically on the provision of explicit, portable universal service funding that is sufficient. Sprint observes, correctly (at 2) that "[n]o entity will willingly enter a market unless the sum of their anticipated revenues exceeds the sum of their anticipated costs. Until that occurs, there will never be vibrant, facilities-based competition in the local exchange." Sprint finds that only 29% of its local customers generate profits today.[10] Sprint also recognizes that "a sizable, implicit, and untargeted fund exists today." Since implicit support cannot be made portable to other carriers, entry into the local market will be preempted until this implicit mechanism can be replaced with explicit funding. Further, a new, explicit fund that is sufficient to replace the existing support need not create any additional burden for customers since support at that level already is built into the system.

In contrast to GTE's Proposal, the plans proposed by other parties do not meet the requirements of the Act. Nor, in fact, do these parties evaluate the results of their plans by any externally measurable objectives. Only BellSouth has proposed an approach which seeks to satisfy the set necessary requirements.

The framework of GTE's Proposal includes, as special cases, the May 1997 plan as well as the current proposal by US West. However, when evaluated against the requirements of the Act, using the current versions of the proxy cost models and the staff's "common" inputs, neither of these plans is sufficient . For example, if the May 1997 plan were implemented without change, GTE estimates that over $5 billion per year in current federal universal service support would not be funded explicitly and made portable to new entrants.[11] Depending on the cost model and inputs chosen, it also may not be possible to meet the necessary requirements with the two benchmark

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[10] A similar point is made by Ad Hoc at 30. Ad Hoc notes that a CLEC would only enter a local market where its revenue would cover its costs.

[11] GTE estimates conservatively that $6.3 billion remains implicit within interstate access rates and that the FCC's May 1997 plan would provide approximately $1 billion using BCPM or HAI cost models.

approach proffered by US WEST. For this reason, GTE has proposed a broader framework that would accommodate additional benchmarks as necessary

A. The Ad Hoc Plan

GTE shares many of the concerns that underlie the Ad Hoc Working Group's proposal (the "Ad Hoc plan"). However, as Ad Hoc itself recognizes, its proposal at best represents just one piece of a sufficient Federal universal service plan. In particular, the Ad Hoc plan is designed to provide support to states, especially those with high costs and/or low revenues. GTE agrees that continued support for state rates is an essential component for the Federal universal service fund, but that is only one of the three requirements which the Federal plan must meet. The Ad Hoc approach gives rise to several concerns.

First, because it focuses exclusively on support to be provided to state commissions, the Ad Hoc proposal, by design, neglects support that is implicit in interstate access rates today. Ad Hoc itself (at 28) recognizes this limitation:

> All of the money would be used by state commissions to reduce intrastate rates.... If the FCC is concerned that access charges include implicit subsidies, it may want to establish additional surcharges and distributions in order to convert existing implicit subsidies in the interstate jurisdiction to explicit subsidies.

The Ad Hoc proposal thus ignores the largest single most important task (in terms of the dollars required) that the Federal plan must perform. Thus, while Ad Hoc takes pride in the fact that its proposal results in a relatively small fund, this is only made possible by the fact that Ad Hoc addresses only a small part of the problem. In fact, the Ad Hoc approach would effectively increase the burden on those who pay interstate rates, since the plan would be funded on a base of interstate revenues, but would not result in any offsetting reductions in interstate rates.

As an approach to determining the amount of support to be provided to the states by the Federal plan – the second of the three requirements outlined above – the Ad Hoc plan has certain strengths and weaknesses. However, even if the Ad Hoc plan were adopted for this purpose, the Federal plan would still have to generate explicit support – *in addition to* that determined by Ad Hoc's calculation --sufficient to replace the $6.3 billion of implicit support provided by interstate access today.

Second, the Ad Hoc plan is based on statewide averaging of universal service support. It shares this feature – and the resulting limitations – with the current HCF. The Ad Hoc plan thus neglects the important role of geographic averaging as a source of implicit universal service support today. Competitive entry will undermine implicit universal service support on a geographically targeted basis. Even if support were sufficient on average, the averaging of support still would preempt competitive entry in high cost areas, in the manner described by Sprint, since the revenue obtained from the provision of local service still would be insufficient to cover local service costs in those areas.

At best, the Ad Hoc plan would have the effect of shifting the average cost for a state down to the nationwide average cost. The variation of costs around the mean, however, differs markedly from one state to the next. Since the Ad Hoc proposal focuses on the average cost and does not consider the *distribution* of costs within or across states, support determined by the Ad Hoc proposal could be insufficient for states that have relatively greater cost variation. For example, suppose that the average cost per line is similar in Arkansas and New Mexico, but the variation of cost around the average is three times greater in New Mexico than it is in Arkansas.[12] In this case, the Ad Hoc plan would shift the average cost of both states down to the national average but still fail to place the two states on an equal footing because the distribution of costs is so different in each state. Thus, even to the extent that federal funding equalizes the average cost across states, under the Ad Hoc plan a low-cost customer in New Mexico still might contribute much more to support high-cost customers in the state than a similarly situated low-cost customer would in Arkansas.[13]

Determining universal service by shifting and "normalizing" the distribution of cost within each state is thus an approach that is inherently fraught with difficulties. Even if the plan were modified to take account of the variance of the state cost distributions, as well as their means, the fact that these distributions are far from regular would still lead to unanticipated results.

In addition, even if the amount provided to each state under the mean-shifting approach were sufficient, the Commission would have to assume that each state commission would adopt a universal service plan which would properly target the funding. For example, if the Commission wishes support to be targeted to small

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12 Results from BCPM 3.1 run at the wire center level with default inputs suggest a line-weighted average cost per line of about $60 for both Arkansas and New Mexico. At the same time, cost variation measured by the standard deviation around the mean is three times greater in New Mexico than it is in Arkansas. Such estimates are sensitive to assumptions and are used here only for illustrative purposes.

13 Colorado recognizes the difficulty of an approach that focuses exclusively on the mean of each state's cost distribution. Colorado asks the Commission to consider a variety of alternatives that would provide greater support to states which, like Colorado, have a wide variation of cost within their borders. The Ad Hoc plan has garnered support only from a subset of states, in part because it does not address the different needs of all the states.

geographic areas, it would be relying on each state to develop the mechanisms to accomplish this. While GTE recognizes the important role states must play in preserving universal service, the Commission has a plenary responsibility to ensure that the requirements of the Act are met through a combination of state and Federal action. GTE submits that it is reasonable for the Federal plan itself to be structured in such a way as to target support to areas where it is needed. It is also reasonable for the Commission, when it provides Federal support to the states, to require that these funds be used to make offsetting reductions in state rates which are providing implicit support today.

The notion that the Ad Hoc plan can provide and target sufficient support is belied by the fact that its relies upon statewide geographic averaging. Ad Hoc (at 27) merely offers an apology for support that is geographically averaged:

> For example, the FCC requires that high cost support be calculated on a fine geographic basis not larger than the wire center. This presupposes that competitive LECs will be free in each state to offer their services on a fine geographic scale and also presupposes that resale rates will be de-averaged at a similar scale.

In fact, the incumbent's rates for resold services, or for UNEs, need not be de-averaged in order for de-averaged USF to provide more effectively targeted support and more efficient price signals to new entrants. To minimize arbitrage opportunities, it would be desirable for state retail, resale, and unbundled network element (UNE) rates to be consistent with one another, and with the USF support that is available. In all practicality, however, it may not be possible to geographically de-average all of those rates in the near future. Despite this potential limitation, it does not follow, as Ad Hoc appears to assume, that USF support cannot usefully be de-averaged. Conversely, GTE has offered in several states the following proposal that enables the Commission to reconcile with local competition its requirements under the Act to make implicit support explicit and assure that all carriers support universal service on an equitable and nondiscriminatory basis.

If universal service support is de-averaged while UNE and retail (resale) rates remain averaged, the primary concern is that large differences may arise between the prices of the UNEs and the support available in a given area.[14] To correct for these geographic inconsistencies, an apportioning mechanism for universal service support may be necessary. Such a mechanism has been adopted in South Carolina.[15] Just as a state commission must determine universal service support by looking at the ILEC's explicit requirements to cover its universal service costs, the same logic should apply consistently to apportion support between the UNE purchaser and provider. Under the South Carolina rule, a purchaser of UNEs may receive universal service support that at most equals the amount it pays for all the UNEs less the basic service rate it may charge to a customer. GTE's proposal, which is similar to the one adopted in South Carolina but includes greater detail, is included in Exhibit 1. [16]

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[14] The cost of a service generally should exceed that of the elements alone simply because there are additional costs incurred to put the elements together and retail the service; however, after allowing for those additional costs, it would be reasonable to expect the UNE and service costs to be close to one another.

[15] Proceeding To Establish Guidelines For An Intrastate Universal Service Fund, South Carolina Docket No. 97-239-C - Order No. 98-201; March 17, 1998.

[16] GTE's proposal was presented in the Rebuttal Testimony of Dr. R. Dean Foreman, February 27, 1998, Before the Public Utility Commission of Texas, Docket No. 18515, Compliance Proceeding for Implementation of the Texas High Cost Universal Service Plan, where it was supported by most parties, including SBC and AT&T.

Also contrary to Ad Hoc's contention, most states have allowed CLECs to define small geographic serving areas. Unfettered by regulation, CLECs also can leverage their flexible service packaging and pricing abilities to target the most desirable customers within an area . CLECs should be free to price, package, and target their offerings, but in order to receive universal service funding they should be required to take on an obligation to serve; this obligation should be defined so as to prevent the CLEC from serving selectively only the customers it wishes, and receiving support for doing so. Although Ad Hoc is correct that a carrier will enter a market only if its expected revenues exceed its expected costs (at 30), it misses the point that the CLEC easily could choose to offer a service package which is more expensive but tailored to attract customers in the target group that the CLEC wishes to serve, such as those with high levels of toll usage. By contrast, an ILEC does not have these capabilities under present regulation. To help achieve the competitive neutrality for universal service that the Commission has embraced, all carriers receiving universal service support should undertake symmetric obligations in return for the same payment per customer in a given area. Specifically for this reason, GTE has, in its earlier comments, urged the Commission to require any carrier to offer, as a condition for the receipt of support, a service which (1) meets the definition of basic service, and (2) is offered at a price no higher than the level found to be "affordable" by the state commission.

Third, while Ad Hoc recognizes the need to reconcile different measures of local service cost, its plan does not do this effectively. The Ad Hoc calculation does not resolve the difference between a forward-looking cost estimate and the embedded cost of service in a given state. Instead, it measures the relative position of that state's mean costs within the distribution of such costs across states. It does this once using a distribution of forward-looking cost estimates, and once using embedded costs, and uses the comparison which produces the lowest difference between the state mean and the national mean. This procedure simply compares how close that state is to the national mean, using two different distributions; it does not provide any information about which estimate of state costs is more accurate.

When this procedure is applied to the proxy cost estimates used by Ad Hoc, the result is that the proxy estimates have little effect on the support that is calculated. Only six of 51 areas (50 states plus the District of Columbia) would receive funding on the basis of their forward-looking economic costs ("FLEC")[17]. In fact, the Ad Hoc group notes (at 32) that because so few states would receive funds based on forward-looking economic cost, the "errors in the FLEC models cause no harm." Thus, to the extent that the Ad Hoc group presents its plan as a stand alone universal service funding mechanism, the FLEC modeling is an arduous and costly process that contributes minimally to the end result.

B. TIAP

The Telecommunications Industry Analysis Project (TIAP) offers a couple of proposals that deserve brief comment.

TIAP Plan 3, Density Zones, focuses on the funding required to support the least dense zone modeled by the BCPM or HAI cost models. While density correlates highly with cost, it is not the sole determinant. TIAP also acknowledges that adding the second lowest density zone doubles or triples the amount of support required. Most

[17] Ad Hoc Table labeled "High Cost Modeling Project - New Support Summary."

fundamentally, this exercise underscores why (1) the basis for funding should be the ILECs' actual costs; and (2) it is imperative that the Commission assure that the funding targeted for a specific geographic area bears a reasonable relationship to what is (a) implicit in rates today and (b) sufficient to preserve and advance universal service in the future.

In contrast, TIAP Plan 5 offers an alternative contribution recovery mechanism that would assess a universal service surcharge on phone numbers in service in each area. This proposal would penalize a customer for choosing multiple connections regardless of whether additional telecommunications revenues are produced using the line, and regardless of the manner in which the line is utilized by the customer, *e.g.*, Internet usage. A telephone number surcharge also would fail to capture revenues associated with any telecommunications services that do not necessitate the assignment of a telephone number, *e.g.*, special access, direct billed calling card products.

C. Time Warner Communications

Whereas proposals by GTE, BellSouth, and Sprint seek to provide sufficient universal service funding and look for credence in what is implicit today in interstate access rates, Time Warner proposes a fundamentally different, income-based, criterion for assessing the need for high-cost support. GTE agrees with Time Warner that targeted subsidies are most effective and for this reason, GTE advocates that all implicit support be made explicit and portable to new entrants on a geographically targeted basis. However, Time Warner's approach is simply detached from the reality of historic state regulation, and therefore cannot usefully address the universal service requirements of the Act.

As the Commission is well aware, the need for universal service support arises when state commissions intervene in the market, requiring carriers to provide service at rates or terms which they would not have chosen voluntarily. In its proposal, Time Warner is arguing, in effect, that states should intervene on a *different basis* than they have historically and do today, and that *the only basis* for a market intervention should be to assist customers with low incomes. The implication of this, which Time Warner does not dwell on, is that customers with average incomes who happen to live in high cost areas would pay very high rates for local service.

Without debating the correctness of Time Warner's proposition concerning what local rates should be considered "affordable," the simple fact is that states have not chosen to confine their market intervention to those customers with low incomes. Instead, the states have required that service be made generally available to all customers in an area at an "affordable" rate. To date, nothing in the Commission's orders on universal service has sought to alter this policy; indeed the Commission has deferred the determination of affordability to the states.

Time Warner's approach assumes, *first*, that the Commission should attempt to alter states' policies with respect to local rates, and, *second*, that an exogenous reduction in Federal universal service funding would translate directly into changes in state rates. Quite simply, Time Warner's assumptions are unrealistic. As long as public policy continues to require affordable, generally available rates, then there must be sufficient, explicit universal service support to maintain those rates. Because adoption of Time Warner's proposal would not change local rates, the proposal amounts to a continuation of implicit support solely in ILEC rates. The Time Warner proposal also is unique among all those put forth in this docket because it would not accomplish *any* of the three necessary requirements for a lawful Federal universal service plan.

IV. MULTIPLE PROPOSALS SUPPORT A SURCHARGE ON TOTAL RETAIL REVENUES FOR THE FEDERAL UNIVERSAL SERVICE FUND.

The Notice also seeks comment on the appropriate method and revenues to recover contributions for high cost support, and GTE has recommended in its proposal that any new compromise between the responsibilities of the Federal plan and those of state plans should include a change in the funding base to envelop total retail revenues: state, interstate, and international. Among the reasons cited by GTE are:

- Interstate rates currently supply a disproportionate share of the implicit support in the system today. A broad contribution base will be necessary for the new Federal universal service fund to be capable of accomplishing the foregoing objectives;
- Arcane state jurisdictional separations already require reform and do not apply accurately to all the telecommunications carriers and service that must contribute to the new explicit Federal universal service fund; and,
- The mandates of the *Act* to foster local competition yet preserve and advance universal service are national in scope and should be borne jointly by the states and the Federal government.

The alternative proposals by Sprint and John Staurulakis, Inc. (JSI), also lend support for a contribution base of total retail revenues. Sprint (at 9) emphasizes that all carriers should support universal service on an equitable and non-discriminatory basis. JSI (at 4) underscores the benefits of a small, uniform national surcharge as opposed to widely varied surcharges by state. While states will be concerned whether their citizens are net contributors or recipients, uniformity as JSI advocates also would help to mitigate arbitrage of state and interstate rates.

The adoption of total revenue (interstate, intrastate and international) for the Federal plan does not mean, as some parties have suggested, that all universal service

VI. CONCLUSION

GTE urges the Commission to adopt a cost model and inputs it will use prior to selecting the benchmarks and percentages in order to appropriately distribute responsibility for universal service support among the Federal and states' plans. GTE and other commenters recommend the Commission adopt a surcharge based on total (interstate, intrastate and international) retail revenues as the appropriate basis for both the contribution method and recovery mechanism. Finally, GTE stresses that the benchmark should be characterized as a "cost" benchmark designed to satisfy the three objectives. The benchmark should not be selected or calculated based on either an average cost or revenue because there is no assurance that such a benchmark will produce and target sufficient support accurately.

GTE's Proposal is the only plan before the Commission that provides the flexibility the Commission will require to assure that the calculated support will be reasonable and sufficient to meet the three requirements once it selects the cost model and inputs. The Commission should use the framework GTE has proposed to develop its Federal universal service plan.

needs would be funded on a national basis. If the Commission adopts a plan sufficient to address the three requirements enumerated above, there will still be a substantial need for state funding mechanisms to replace the implicit support provided by state rates today. These mechanisms will vary in size to reflect the circumstances of the different states.

V. THE FEDERAL BENCHMARKS SHOULD BE CHARACTERIZED AS COST BENCHMARKS.

The Notice seeks comment as to whether the Federal plan should employ a benchmark based on cost, instead of revenue. Fundamentally, the Commission should select parameters for the funding mechanism to produce and accurately target sufficient, explicit funding. As described previously, there is broad-based support among the proposals for providing sufficient funding to states and implementing a flexible mechanism to target funding. In search of a systematic basis for varying support among states, the alternatives put forth by Colorado (at 3) and South Dakota (at 4) offer state specificity based on an average or ratio calculated using costs or revenues. As GTE underscored in its proposal, the benchmarks should not be selected by calculating either an average cost or revenue because there is no basis to assure the calculation will produce and target sufficient support pursuant to the foregoing objectives. Once benchmarks have been selected which satisfy the policy objectives, however, they should be characterized as cost benchmarks. The benchmarks would thus represent levels of local service cost at which the Commission would intervene to provide funding from the Federal plan. They would not, and should not, represent a finding by the Commission that any particular amount of revenue will be available from rates in a given area to support those costs.

Dated: May 15, 1998

Respectfully submitted,

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EXHIBIT 1

APPORTIONMENT OF SUPPORT WHEN A UNIVERSAL SERVICE PROVIDER[1] PURCHASES UNES

1) **Defining terms**

Suppose the total cost of providing basic local service in a given area is estimated by the USF cost model and equals TC. The total cost, TC, can be divided into the retailing cost (RET) and the remaining wholesale cost (WC), so

$$TC = RET + WC.$$

The carrier that serves the end user will incur the retailing cost. Suppose further that for the universal service calculation the Commission selects a single cost benchmark, denoted BMARK.[2] In areas where the USF cost is greater than the benchmark, the support is the difference between the two:

$$\begin{aligned} \text{Support} &= TC - BMARK \\ &= (RET + WC) - BMARK \end{aligned}$$

Summing the prices of all the UNEs that comprise basic local service produces a total that will be referred to as SUMUNE. Since UNE prices are set on a

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[1] For this discussion, GTE will use the term Universal Service Provider ("USP") to refer to a carrier that is certified as an eligible telecommunications provider ("Eltel"), that takes on an obligation to serve and that satisfies any other requirements for the receipt of support from the Federal plan.

[2] With no loss of generality, a single-benchmark calculation like that of the Commission's May 1997 plan is described; the same apportionment could be carried out with a plan that employs more than one benchmark. In a parallel state mechanism, the state would be comparing the estimated cost with the revenue associated with basic local service, and apportioning state support in a similar fashion.

geographically averaged basis, in high cost areas the sum of the UNE prices will be less than WC, the USF cost net of retailing and recombining costs.

2) **Apportioning support when all UNEs are purchased**

When the USP purchases all of the UNEs that comprise basic local service, the USP's cost of providing basic local service is the sum of the UNE prices plus the retailing and recombining cost, (SUMUNE+RET). The support the reseller[3] should receive is the difference between its own cost and the cost benchmark, wherever that difference is positive:

Reseller Support = (SUMUNE +RET) – BMARK.

The reseller would not receive support where its costs were below the benchmark, that is, where (SUMUNE + RET) < BMARK.

The underlying carrier would receive the remaining part of the support:

Underlying Carrier Support = Support - Reseller Support

= [(WC + RET) - BMARK] - [(SUMUNE + RET) - BMARK]

= WC – SUMUNE.

This support compensates the underlying carrier for the cost of providing the UNEs in the high-cost area. The cost recovered through the price of the UNEs equals the sum of the UNE prices. Note that if the sum of the UNEs (SUMUNE) is greater than the wholesale cost (WC) then the reseller would receive all of the available support.

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[3] For purposes of this discussion, the term "reseller" means the USP that purchases UNEs. This is not meant to suggest that the USP is engaging in full service resale; the term is used simply to avoid having to repeat "USP that purchases UNEs."